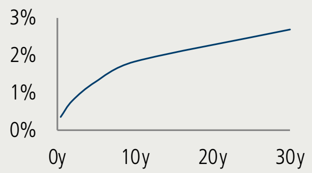
DAILY FIX

JANNEY FIXED INCOME STRATEGY

APR 28, 2016

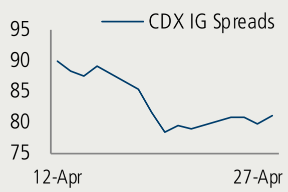
Market Close

	Yld	Prev.	Chg.
2yr	0.82	0.86	-(0.04)
5yr	1.32	1.39	-(0.07)
10yr	1.85	1.93	-(0.08)
30yr	2.70	2.75	-(0.05)



MBS	Yld	Price	Chg
FN 3.0%	2.62%	102-10	+11
GN 3.0%	2.46%	103-8	+08

Credit	Close	Chg
CDX IG	79.8bp	-1.0bp
CDX HY	$103.4	$0.3



Muni	Yld (5%)	% Tsy	Chg.
2yr	0.61	74%	4%
10yr	1.74	94%	3%
30yr	2.75	102%	2%

Source: MMA

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Day Ahead:

- *Rates: treasury supply resumes with $28 billion 7yr sale plus $15 billion 2yr FRN sale; take-up may be softer on 7s*
- *Eco: 1Q GDP (Janney +0.4%) likely to fall short of consensus, though a strong March trade report y'day adds upside risk*
- *Credit: Earnings parade continues w/Ball Corp (big miss), Aetna (slight beat), Time Warner Cable (slight beat)*

Market Review:

Although the Federal Reserve issued an FOMC statement relatively close to our expectations, the market interpretation was highly dovish, leading to gains across the yield curve, gains that followed from seven consecutive sessions of losses. Yields gapped lower by 1 – 2 basis points at the open of Asian trading hours, and there were reports of central bank and money manager buying in Treasuries. The buying theme continued through the end of the overnight as well as the beginning of US trading hours—though, of course, the main event wasn't until 2PM EDT. At 2, the FOMC released its April FOMC statement, and while that statement dropped the line about global financial and economic risks, it failed to add a "balance of risks" line, which preceded the December rate hike. That absence drove buying across the curve, and yields ended well lower, with the ten year Treasury yield falling 7.5 basis points to 1.85% and the two year yields falling 4.5 basis points to 0.82%. Overnight, the Bank of Japan whiffed and failed to add any new stimulus, despite another leg downward in economic activity; global equities are selling off, and we've already seen flight-to-quality buying in Treasuries, despite the early hour.

About twelve months ago, the BEA began publishing an early estimate of the import/export balance with the advance goods trade balance report. While the advance report doesn't cover all imports or exports, it does cover the most volatile component of international trade, which makes it quite useful for looking at changes to GDP. For March, the goods trade balance unexpectedly narrowed to -$56.9 billion, an improvement of +$6.5 billion versus February's numbers, returning the first quarter much closer to the trend level realized in late-2015. In other words, it looks like the trade balance only temporarily widened in February for whatever reason—perhaps it was the timing of the Lunar New Year holiday, weather, or some other unobservable temporary factor. The better goods trade balance puts some upside risk to our +0.4% 1Q GDP forecast (as much as two tenths upside to that number, actually), and confirms our assessment that weak 1Q GDP growth would likely be transitory. *–Guy LeBas*

Recent unfavorable responses to mega-mergers by antitrust regulators—e.g., pharma company **Pfizer**'s (A1/AA/A+) terminated purchase of **Allergan** (Baa3/BBB-/BBB-) and oilfield services firm **Halliburton**'s (A2/A/A-) combination with **Baker Hughes** (A2/A/NR)—has not stopped some companies from pursuing large-scale acquisitions. Medical products firm **Abbott Laboratories** (A2/A+/A) announced the purchase of medical devices firm **St. Jude Medical** (Baa2/A-/A-) for $25 billion this morning. Abbott plans to assume St. Jude's debt outstanding, in addition to issuing about $13 billion in new medium- and long-term debt to finance the cash portion of the transaction. Management indicated it is "committed to maintaining an investment grade credit rating" with pro forma leverage falling from 4.5x to 3.5x in 2018. As we've commented previously, not only are firms taking advantage of the low rate environment, but also they are masking sluggish organic top line growth via acquisitions and other financial engineering. Abbott spun off its pharma business into **AbbVie** (Baa1/A/NR) in 2013, and has been acquisitive since; for example, it announced the purchase of life sciences firm **Alere** (B2/B/NR) in February for $8.0 billion. *–Jody Lurie*

Puerto Rico faces a large debt service hurdle on Monday, May 2nd when about $470 million of principal and interest payments for various Puerto Rico issuers come due. As Moody's explains in its April 25th report titled "Puerto Rico Will Default on More Securities in May, Regardless of US Action," PR Government Development Bank defaults are very likely, with the $422 million PR GDB principal and interest payments representing the bulk of money due on May 2nd. On April 6th, Puerto Rico's governor signed legislation authorizing the governor to declare a moratorium on paying debt service, as he feels necessary, in order to continue providing essential services to island residents. Yesterday (April 27th), a spokesman for the governor said he plans to invoke the moratorium, thus placing Puerto Rico on the path to near-certain default on Monday.

A bill from the US Congress to address the island's fiscal crisis has stalled in committee, with House leadership now targeting July 1st as the potential delivery date for legislation, coinciding with the next major debt hurdle, a July 1st payment totaling $2 billion across various issuers, including $800 million of general obligation debt. Smaller Puerto Rico issuers, PR Infrastructure Financing Corp and PR Public Finance Corp, have already defaulted. Barring Congressional legislation establishing some type of debt restructuring framework, cascading defaults will lead to extensive litigation. We believe stakeholders (bondholders, residents, pensioners, PR government, US government) will be best served by the orderly process which Congressional action could provide, rather than the chaotic scramble that could ensue once the litigation battle begins. Its $70 billion debt load notwithstanding, Puerto Rico's biggest challenge is its contracting economy and the resultant persistent pace of outmigration. These larger, critical issues can only be addressed when Puerto Rico's fiscal situation is stabilized. *–Alan Schankel*

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